DCAA Contract Audit Manual (CAM)
(DCCAM 7640.1)

Chapter 11
Performance Audits and
Agreed-Upon-Procedures Engagements

August 28, 2026

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11-100 Performance Audits **

11-101 Introduction **

Performance audits must be conducted in accordance with the requirements and application guidance in GAGAS chapters 8 and 9 to ensure their engagements comply with the relevant professional standards. Performance audit objectives range from narrow to broad and involve varying types and quality of evidence. The auditor should identify and use suitable criteria based on the audit objectives to adequately plan the work necessary to address those objectives and design the methodology to obtain sufficient appropriate evidence that provides a reasonable basis for the findings and conclusions based on the audit objectives. Historically the type of performance audits DCAA has performed have been in the area of Operations Audits.

11-102 Audit of Operations of Major Contractors **

11-102.1 Audit Plan **

If the Government has a significant interest in a contractor's operations, the audit plan should provide for ongoing audits of related management system areas. The plan should support timely reporting on important cost areas and be broad enough to cover the contractor's operations that affect Government contract performance.

11-102.2 Audit Approach **

a. A contractor's reported costs that reflect actual experience come from the contractor's official accounting records, which are the result of its internal control and accounting systems. These recorded costs show how management's policies, decisions, and controls affect operations and spending. Based on the idea that the whole is the sum of its parts, data from these records may be accepted when costs and financial information are supported by:

1. Prudent management policies and decisions
2. An efficient organization with effective management control over operations
3. A sound, reliable system for accumulating accounting and financial data

b. Based on this principle, the total audit approach focuses heavily on:

- How prudent management is in setting policies and making decisions
- How effectively costs are controlled
- How much reliance can be placed on the accounting and other financial information

11-102.3 Audit Program (Operations Audit) **

a. Plan the audit to keep audit risk acceptably low by assessing significance and risk and using that to set the scope and method of the audit.

b. Organize the audit program by specific functions or areas so procedures are logically arranged for evaluating and reporting results.

c. Use suitable criteria that fit the audit objectives and are relevant, reliable, objective, and understandable. If laws, regulations, or policies set the criteria, they are generally considered suitable unless there is reason to consider otherwise. See the 2024 GAGAS 8.18 for examples of criteria.

11-103 Planning Considerations **

a. The audit plan for major contractor operations is primarily designed to seek out and identify those areas where the contractor's practices are wasteful, careless, and inefficient and result, or may result in unreasonable costs and unsatisfactory conditions in performing Government contracts; and to report such matters to those responsible for taking action to correct or improve the condition. A procurement agency's special interest in certain areas of the contractor's operations should be considered in audit planning.

b. FAR 31defines what makes a cost reasonable on Government contracts. Auditors must carefully identify unreasonable costs by understanding the contractor's operations and industry practices, while recognizing that the contractor's interests may differ from the Government's. For example, from the contractor's viewpoint it may be more prudent for the contractor to rent rather than purchase an item of equipment even if the action results in greater contract cost.

c. Audit procedures should give the auditor a clear understanding of how the contractor manages operations, makes key business decisions, uses employees and resources, and controls costs. The auditor should be able to judge whether expenses are necessary, practices are sound, and decisions are prudent and consistent with established practices. The auditor should understand the process upon which the management decisions are made by the contractor.

d. In terms of an audit technique, this approach must be geared to inquire into those management and operational decisions which affect the nature and level of costs being proposed and incurred under Government contracts. The knowledge gained forms the basis for constructive recommendations to improve the contractor's internal control structure and the economy and efficiency of contractor operations.

11-104 Cost Avoidance Recommendation Resulting From Operations Audits **

a. The report should include cost avoidance recommendations even if the contractor disagrees with the audit results. If the auditor identifies a measurable opportunity to reduce costs, the report should include a realistic estimate of the savings. Cost avoidance should be estimated conservatively, net of any offsetting implementation costs, for a reasonable period of time during which the audit team believes the cost savings can continue to be recognized by the Government. The audit team should document the rationale behind the time period for the cost savings in the working papers. The savings may be one-time, program-specific, equipment-related, or recurring annually.

b. Cost avoidance represents the savings achieved by implementing recommended practices compared to current costs.

To calculate this:

1. **Determine the Difference:** Calculate the difference between current costs and the lower costs of recommended practices or expenditures.
2. **Timeframe:** Base this calculation on current year costs and reasonably estimated future costs for up to six years.
3. **Gross Savings:** Compute the total savings across all of the contractor's operations.
4. **Deduct Implementation Costs:** Subtract any implementation and installation costs from these total savings *before* allocating them. These costs must be clearly shown in the audit report.
5. **Prorate to Government Contracts:** Allocate the remaining net savings to government

contracts (including fixed-price, flexibly-priced, and subcontracts) based on their percentage of the contractor's total sales.

11-105 Conferences and Reports on Operations Audits **

See Chapter 4 for guidance on entrance, interim, and exit conferences with the contractor. Promptly after completing each operations audit, prepare and distribute a report in accordance with GAGAS Chapter 9, regardless of findings.

11-200 Application of Agreed-Upon Procedures **

11-201 Introduction **

a. This section contains guidance on performing agreed-upon procedures engagements. An agreed-upon procedures engagement is one in which an auditor is requested to issue a report of findings based on specific procedures, agreed-upon by the auditor and requestor, performed on an assertion or a subject matter. An agreed-upon procedures engagement is appropriate for situations where the requestor wants information on a subject matter or assertion, generally relative to specific criteria, but does not require an opinion, recommendations or negative assurance. Instead, users of the report assess for themselves the procedures and findings reported by the auditor and draw their own conclusion based on the auditor's work.

b. Under GAGAS, DCAA may perform an agreed-upon procedures engagement if (1) the subject matter or assertion to which the procedures are to be applied is subject to reasonably consistent measurement, (2) the requestor and DCAA agree on the nature, timing, and extent of the procedures to be applied, including the criteria to be used and (3) the requestor assumes responsibility for the sufficiency of the procedures. Agreed-upon procedures engagements are conducted in accordance with GAGAS 7.78 – 7.85, the Statements on AT-C section 105, AT-C section 215, and the relevant portions of AT-C section 315.

11-202 Agreed-Upon Procedures **

In an agreed-upon procedures engagement the requestor assumes responsibility for the sufficiency of the agreed-upon procedures since the requestor determines, based on their specific needs, what procedures should be performed. Directorates should modify their quality control and AUP monitoring processes to require Branch Manager and RAM, if appropriate, approval of the proposed procedures prior to agreement with the requestor and for review of draft AUP reports before issuance. Such approvals must be documented in the working papers. The auditor is responsible for carrying out those procedures. In planning an agreed-upon procedures engagement the auditor should:

- Understand the requestor's objectives,
- Understand the difference between appropriate and inappropriate agreed-upon procedures, and
- Establish an agreement with the requestor on the terms of the engagement.

11-202.1 Understanding the Requestor's Objectives **

a. Requests for DCAA services vary, depending on specific circumstances and customer needs. The auditor should inquire about the requestor's objectives and then discuss with the requestor the procedures which will accomplish those objectives. The auditor should clarify exactly what the requestor needs and structure the engagement appropriately. Other types of audit services may be more appropriate to satisfy the requestor's objectives. Requests for procedures that require the auditor to make determinations based on auditor judgment (e.g., reasonableness) or provide recommendations or opinions should not be performed as an agreed-upon procedures engagement. Agreed-upon procedures acknowledgement letters include a list of sample questions the auditor may use to assist in determining the appropriate engagement.

b. If applicable, the auditor and requestor should also explicitly discuss the use of a technical specialist. The auditor should document the discussion.

11-202.2 Appropriate Agreed-Upon Procedures **

Auditing standards limit the type of work that can be performed as agreed-upon procedures. Agreed-upon procedures must be clear, objective, and not require the auditor to give an opinion or make recommendations. Avoid vague terms (such as Note, Review, General review, Limited review, Evaluate, Analyze, Check, Test, Interpret, Verify or Examine) unless they are clearly defined. Use precise action words like Inspect, Confirm, Compare, Trace, Inquire, Recalculate, Observe, or Mathematically Check so the procedures produce consistent findings using the established criteria.

11-202.3 Establishing an Agreement on the Terms of the Engagement **

a. GAGAS requires auditors and requestors to clearly agree on the engagement terms. DCAA documents this in an acknowledgment letter that lists the agreed-upon procedures and any agreed materiality limits. The letter should be issued only after both parties agree on the procedures. The engagement should not proceed if the procedures are not agreed to or if the requestor does not accept responsibility for their sufficiency. If procedures change, document the requestor's acceptance in the working papers, and issue a revised acknowledgment letter if the changes are significant.

b. The auditor should inform the requestor about any known CAS, FAR, or DFARS issues that could significantly affect the agreed-upon procedures. The auditor does not need to perform work beyond the agreed procedures. Document these discussions in the working papers, include them in the acknowledgment letter if known, and report them under "Report on Other Matters."

c. If there are restrictions limiting the agreed-upon procedures, the auditor should try to revise the procedures with the requestor. If no agreement is reached, the auditor should report the restriction or withdraw if it significantly limits the work.

d. Before changing an examination to agreed-upon procedures, the auditor should follow the disclaimer of opinion guidance in Chapter 2. An examination cannot be changed just to avoid reporting a scope limitation or a disclaimer of opinion.

11-203 Agreed-Upon Procedures Report **

This section provides guidance for preparing application of agreed-upon procedures reports in accordance with GAGAS.

11-203.1 Nature of Agreed-Upon Procedures Reports **

In an agreed-upon procedures engagement, the auditor issues a written report on findings from specific procedures agreed to by the auditor and requestor and applied to the contractor's subject matter or assertion. The auditor should report only on agreed procedures that the requestor has accepted as appropriate for the engagement's purpose. Agreed-upon procedures are not an examination, review, or advisory service. The report helps the requestor evaluate a subject matter or assertion by presenting findings based on agreed procedures and criteria chosen for a specific purpose.

11-203.2 Agreed-Upon Procedures Report Format and Contents ****

a. Prepare reports following the standard aspects of report preparation and the professional standards for reporting, as shown in CAM Chapter 10. The report should contain all necessary and pertinent information to be fully responsive to the needs of the recipient. Reports should be prepared using the following format:

- Report Cover Sheet *
- Table of Contents *
- Executive Summary *
  - About [Contractor's Name]*
  - About this Agreed-Upon Procedures Engagement*
  - What We Found*
- Report on [Brief Description of the Agreed-Upon Procedures]*
  - Management's Responsibility*
  - Auditor's Responsibility*
  - Scope of Application of Agreed Upon Procedures*
  - Results of Application of Agreed-upon Procedures*
- DCAA Personnel and Report Authorization *
- Report Distribution and Restrictions *
- Exhibits
- Appendixes

* Required in every report regardless of type.

c. DCAA limits the word "audit" to reports on examinations. Therefore, the word "audit" is not included in the report number, the report title, the section headings, or the report header. Instead, the words "Application of Agreed-Upon Procedures" are included in the section headings. The use of the term "engagement" rather than "audit," "examination," or "review," is more appropriate to describe the work performed by DCAA in an agreed-upon procedures engagement.

d. Example report language is included in the report shells and the working papers A and A-01 depending on the agreed-upon procedures engagement for activity codes 17800, 17900, 28000 and 29000.